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8 **UNITED STATES BANKRUPTCY COURT**
9 **SOUTHERN DISTRICT OF CALIFORNIA**
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12 In re) Bankruptcy Case No. 00-00742-A7
13 LPM CORPORATION, a California)
14 Corporation, dba LA JOLLA) MEMORANDUM DECISION
15 PATIO & MATTRESS,)
16 Debtor)
17 _____)

18 **I.**

19 **INTRODUCTION**

20 Kir Temecula L.P. (“Kir Temecula”) moves for an order directing North
21 County Bank to release \$33,529.08 in funds to satisfy the levy on its writ of execution.
22 The funds are in the former debtor in possession account of LPM Corporation, dba
23 La Jolla Patio & Mattress (“Debtor”). Kir Temecula levied this account to collect the
24 remaining amounts owed under its order compelling payment of rent. The Debtor
25 converted the case to one under chapter 7 before the levy was completed.

26 Kir Temecula contends it can enforce the levy because the automatic stay
27 was lifted in the chapter 11 case. The conversion did not reimpose the stay; nor did
28 it operate to invalidate the order which required immediate payment. Further, Kir
Temecula argues the Debtor paid some of its landlords but not others in violation of

1 § 365(d)(3).¹ The Debtor cannot choose whom to pay, and cannot defy the order
2 compelling payment when it had the funds to comply.

3 The chapter 7 trustee (“Trustee”) opposes the motion because the estate
4 is administratively insolvent. Given this changed circumstance, he contends immediate
5 payment would grant Kir Temecula an improper superpriority in violation of § 726(b).
6 This section mandates the chapter 7 administrative creditors must be paid before the
7 chapter 11 administrative creditors. He contends Kir Temecula should be paid *pro*
8 *rata* with the other unpaid chapter 11 administrative creditors to the extent any funds
9 remain.

10 Additionally, the Trustee does not believe the order was defied. He
11 requests judicial notice of the Debtor’s motion for partial relief from the order due to
12 the estate’s unanticipated insolvency. He believes that motion had substantial merit,
13 but was mooted by the conversion. Having had the opportunity to review the case law
14 and having duly considered the arguments made in the pleadings, the Court denies Kir
15 Temecula’s motion.

16 II.

17 FACTUAL BACKGROUND

18 The Debtor filed a chapter 11 petition on January 26, 2000. At that time,
19 the Debtor operated approximately forty La Jolla Patio & Mattress retail stores
20 throughout Southern California. During the first sixty days, the Debtor remained
21 current on only a few of its leases notwithstanding the statutory mandate of
22 § 365(d)(3). Kir Temecula is one of the landlords who was not paid.

23 On March 20, 2000, Kir Temecula moved for an order compelling timely
24 payment of postpetition rent or rejection and immediate surrender of the premises
25

26 ¹ Hereinafter, all section references refer to title 11 of the United States Code
27 (“Bankruptcy Code”) unless otherwise specified.

1 (“Surrender Motion”). The Debtor did not file opposition to the Surrender Motion
2 because it intended to reject the lease. Accordingly, the motion was granted as
3 unopposed.

4 On May 9, 2000, the Court entered its order granting the Surrender
5 Motion. The order (hereinafter “Surrender Order”) deemed the lease rejected as of
6 April 30, 2000 and compelled immediate surrender of possession. Further, it ordered
7 the Debtor to pay Kir Temecula \$43,529.08 within two weeks of entry of the order.
8 The order does not provide a remedy in the event of noncompliance.²

9 On May 25, 2000, the Debtor made a partial payment of \$10,000. The
10 next day, the Debtor filed a motion for partial relief from the Surrender Order
11 (hereinafter “Motion for Partial Relief from Order”) which was set for hearing
12 July 6, 2000. The motion sought relief under Federal Rule of Civil Procedure 60(b)(1)
13 based upon mistake, inadvertence and excusable neglect. Specifically, the Debtor
14 claimed it should be relieved from the order due to the changed circumstance of the
15 Debtor learning it may be administratively insolvent. The Debtor claimed it did not
16 know of this circumstance when it elected not to file opposition to the Surrender
17 Motion.³

18 Kir Temecula waited the two weeks required by the Surrender Order, and
19 when the Debtor failed to pay the ordered amount, obtained a writ of execution from
20 the Clerk of this Court. Thereafter, it caused a notice of levy to be served on North
21

22
23 ² Kir Temecula’s Exh. 1.

24 ³ The Declaration of Richard M. Kipperman filed in support of the Motion for
25 Partial Relief from Order sets forth the Debtor’s cash and the unpaid administrative
26 expenses as of May 25, 2000. He concludes that, due to unanticipated administrative
27 expenses, the estate may have insufficient cash to pay administrative creditors in full.
Accordingly, he could only pay Kir Temecula \$10,000 without crippling the estate’s ability
to operate. [Kipperman Decl. filed May 26, 2000 at ¶¶ 7-10].

1 County Bank and Robbins & Keehn APC, Debtor's counsel. The Debtor converted
2 the case to one under chapter 7 before the levy was completed.⁴ As a result of the
3 conversion, the Motion for Partial Relief from Order was taken off calendar. North
4 County Bank has frozen the account pending a ruling on this motion.

5 **III.**

6 **ISSUES PRESENTED**

7 1. Whether the automatic stay precluded Kir Temecula from levying the
8 Debtor's bank accounts.

9 2. Whether immediate payment would grant Kir Temecula superpriority
10 over chapter 7 administrative creditors in violation of § 726(b).

11 3. Whether the Surrender Order entitles Kir Temecula to superpriority
12 over other unpaid chapter 11 administrative creditors.

13 **IV.**

14 **LEGAL ANALYSIS**

15 **A. The Automatic Stay Precluded the Levy.**

16 Kir Temecula argues it was free to levy the Debtor's bank account
17 because the conversion did not reimpose the automatic stay. It cites *In re State*
18 *Airlines, Inc.*, 873 F.2d 264, 268 (11th Cir. 1989), for the proposition that conversion
19 does not reimpose the automatic stay. The appellants in *State Airlines* sought and
20 received an order lifting the stay in the chapter 11 case. 873 F.2d at 265. Having
21 already received an order, the court of appeals held no additional stay relief was
22 necessary because conversion did not reimpose the automatic stay. *Id.* at 268.

23 In the present case, Kir Temecula incorrectly assumes it had an order
24 lifting the stay in the chapter 11 case. The Surrender Order nowhere purports to lift
25 the automatic stay. Rather, the stay was lifted only to the extent provided in § 362(c).

26
27 ⁴ Declaration of George B. Blackmar filed July 21, 2000 at ¶¶ 8-9.

1 This section provides the stay ends when the property is no longer in the estate, or
2 the earliest of the time the case is closed or dismissed. *In re Pintlar Corp.*, 124 F.3d
3 1310, 1313 (9th Cir. 1997). Thus, in this case, the Surrender Order caused the stay
4 to be lifted to permit recovery of the surrendered premises because they were no
5 longer in the estate. But it did not lift the stay to permit seizure of the other property
6 that remained in the estate. The Debtor's bank account undisputedly remained in the
7 estate. Therefore, the automatic stay continued to protect this account.

8 At the hearing, Kir Temecula argued Federal Rule of Bankruptcy
9 Procedure 9014, which incorporates Federal Rule of Bankruptcy Procedure 7069 and
10 Federal Rule of Civil Procedure 69, permits enforcement of the Surrender Order
11 notwithstanding the automatic stay. These rules collectively provide that an order in
12 a contested matter is enforceable by writ of execution, unless the court directs
13 otherwise. Because the Court did not direct otherwise, Kir Temecula contends it acted
14 within the law in obtaining a writ of execution.

15 This Court agrees Kir Temecula can obtain a writ of execution, but this
16 procedural rule does not authorize Kir Temecula to levy on property protected by the
17 automatic stay. Such an interpretation would create a conflict between the Bankruptcy
18 Rules and the Bankruptcy Code. Where there is a conflict between the Bankruptcy
19 Rules and the Bankruptcy Code, the Bankruptcy Code controls. *In re Greene*, 2000
20 WL 958885, *5 (9th Cir. July 12, 2000); *In re Pioneer Finance Corp.*, 246 B.R. 626,
21 633 (D. Nev. 2000). Accordingly, Kir Temecula is not entitled to the funds in the bank
22 account because its levy violated the automatic stay.

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1 **B. Kir Temecula Is Not Entitled To Priority Over Chapter 7**
2 **Administrative Expenses.**

3 Kir Temecula would likely be satisfied with an order directing immediate
4 payment from any of the estate's assets. Because there may be insufficient assets to
5 fully pay chapter 7 administrative creditors, this would give Kir Temecula superpriority
6 over the chapter 7 administrative creditors even though § 726(b) mandates the chapter
7 7 administrative creditors must be paid first. Kir Temecula contends § 365(d)(3)
8 affords the landlord superpriority where it promptly obtains a court order enforcing
9 its rights under this section.

10 The case law is split on this issue, and there is no controlling Ninth Circuit
11 authority.⁵ The majority of courts hold the landlord is entitled to immediate payment
12 except when it appears the estate is administratively insolvent. *See In re Microvideo*
13 *Learning Systems, Inc.*, 232 B.R. 602, 605-6 (Bankr. S.D.N.Y. 1999)(siding with the
14 "vast majority" of courts that adopt the majority view); *In re J.T. Rapps, Inc.*, 225
15 B.R. 257, 261 (Bankr. D. Mass. 1998)(summarizing the competing views and adopting
16 the majority view); *In re The Tandem Group, Inc.*, 61 B.R. 738, 741-42 (Bankr. C.D.
17 Cal. 1986)(holding the landlord is not entitled to superpriority). These courts reason
18 the language of § 365(d)(3) requires payment of the rent at the contract rate as it comes
19 due. However, it does not provide the remedy for nonpayment is superpriority.
20 Where the estate is administratively insolvent, immediate payment of the unpaid rent
21 conflicts with § 726(b). It would improperly grant the landlord a *de facto* superpriority
22 where none was explicitly provided in the statute. *Microvideo*, 232, B.R. at 607-8; *J.*
23 *T. Rapps*, 225 B.R. at 263-4. As *J.T. Rapps* explained:

24 _____
25 ⁵ In *In re Pacific-Atlantic Trading Co.*, 27 F.3d 401, 405 (9th Cir. 1994), the Ninth
26 Circuit Court of Appeals ordered immediate payment of the rent at the contract rate as an
27 administrative expense, but specifically stated it expressed no opinion as to whether this
28 administrative expense was entitled to superpriority.

1 In at least three sections of the Bankruptcy Code, Congress
2 explicitly provides a claim with blanket priority over another
3 class of claims. Section 726(b) provides such priority to
4 Chapter 7 administrative claims over Chapter 11
5 administrative claims. Section 364(c)(1) allows the court to
6 afford superpriority status to postpetition borrowings when
7 the debtor is unable to obtain unsecured credit. And
8 section 507(b) claims receive superpriority status when
adequate protection under § 361 fails. [Citations omitted]
Congress clearly understood how to provide superpriority
status for claims it sought to prefer. “In absence of such
Congressional direction with regard to section 365(d)(3)
claimants ‘it would be inappropriate to imply the existence
of an automatic superpriority status.’” [Citations omitted]

9 *Id.* at 263.

10 The *J.T. Rapps* court recognized a landlord is not without a remedy. The
11 landlord may: (i) file a motion compelling payment of the rent; (ii) move for an order
12 to immediately surrender the premises; (iii) file a motion for relief from stay to have the
13 estate representative evicted from the premises; or (iv) move for an order to convert
14 the case to one under chapter 7. *Id.* However, there is no evidence Congress
15 intended the remedy of superpriority at the expense of those not responsible for the
16 offense. *Id.* at 264.

17 Kir Temecula contends it exercised its remedy by obtaining an order
18 compelling payment of the rent. Therefore, the Court should follow the minority view
19 in this case. The minority view treats the rent as an operational expense and affords
20 the landlord superpriority if the landlord acts promptly. *In re Pudgie’s Dev. of N.Y.*,
21 223 B.R. 421, 427 (Bankr. S.D.N.Y. 1998)(“*Pudgie’s II*”), *aff’d* 239 B.R. 688
22 (S.D.N.Y. 1999)(“*Pudgie’s III*”)⁶; compare *In re Brennick*, 178 B.R. 305, 307-8
23 (Bankr. D. Mass. 1995)(granting superpriority without addressing the requirement of
24 prompt action).

25
26 ⁶ Kir Temecula cited *Pudgie’s II* in its pleadings. However, *Pudgie’s II* is better
27 understood in conjunction with *Pudgie’s III* which explains the factual basis for the ruling.

1 In *Pudgie's III*, the district court recognized it was improper to grant the
2 landlord superpriority over the chapter 7 administrative expenses. 239 B.R. at 695.
3 Accordingly, it indicated the landlord cannot sit back and allow its claim to accrue.
4 *Id.* at 695. The landlord must promptly enforce the debtor's § 365(d)(3) obligations
5 to be entitled to immediate payment. *Id.* Because the landlord allowed its claim to
6 accrue for seventeen months, it was not entitled to an order directing immediate
7 payment. *Id.* at 697.

8 In contrast, the *Brennick* court utilized § 105(a) to grant the landlord the
9 remedy of superpriority. The court recognized § 365(d)(3) requires "timely" payment
10 of the rent, but does not provide a remedy in the event of nonpayment. 178 B.R. at
11 307-8. It reasoned use of § 105(a) was appropriate to further the statutory mandate
12 that the landlord must be "timely" paid. *Id.* at 308. The *Brennick* court did not
13 address the propriety of using § 105(a) to override § 726(b). Further, it did not
14 specify the landlord must act promptly.⁷

15 The Court declines to follow the minority view in this case. The Court
16 will not imply superpriority over chapter 7 administrative creditors where § 365(d)(3)
17 does not provide this remedy. Such a result ignores the mandated priority of § 726(b),
18 and it unfairly harms others who are not responsible for the offense. No professional
19 would agree to serve in the chapter 7 case if a chapter 11 administrative creditor could
20 sweep up the remaining assets of the estate.

21 Moreover, even under *Pudgie's III*, Kir Temecula is not entitled to
22 immediate payment of its accrued claim. Kir Temecula promptly enforced the
23 Debtor's § 365(d)(3) obligations, but a claim of \$33,529.08 has accrued. *Pudgie's*
24 *III* recognized the court can enforce the debtor's § 365(d)(3) obligations, but it cannot
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26 ⁷ The landlord was only owed \$4,960.50 after thirteen months. Accordingly,
27 prompt action may not have been an issue.

reorder the priorities once a “claim” has accrued. 239 B.R. at 695.⁸

C. **Kir Temecula Is Not Entitled To Priority Over Chapter 11 Administrative Expenses.**

Additionally, the Court declines to award Kir Temecula priority over the unpaid chapter 11 administrative expenses. As more fully explained above, § 365(d)(3) is devoid of any grant of superpriority and it is inappropriate to imply such a remedy simply because Kir Temecula acted promptly.

Kir Temecula argues that another case decided in this district took a different position. Specifically, *In re Leisure Time Sports, Inc.*, 189 B.R. 511 (Bankr. S.D. Cal. 1995), held administrative rents paid under § 365(d)(3) are entitled to superpriority status. [Surreply at 3 n.2] This overstates the holding of *Leisure Time Sports*. In that case, the court addressed the issue of disgorgement of rents that were already paid. It held a landlord cannot be compelled to disgorge properly paid § 365(d)(3) rent payments when a case subsequently proves to be administratively insolvent. *Leisure Time Sports*, 189 B.R. at 513. Although the court did indicate the landlord is entitled to superpriority, it said this in the context of disgorgement which is very different than the situation in this case. Accordingly, *Leisure Time Sports* does not conflict with the holding of this case.

Finally, the Court recognizes Kir Temecula would have been paid had the Debtor complied with the deadline in the Surrender Order. While the Court is not pleased with the Debtor’s noncompliance, it did attempt to seek relief from this order due to changed circumstances and risked the possibility of being cited for contempt had such a motion been made. Kir Temecula’s own cited case recognized the remedy for nonpayment is a motion for contempt. *See Pudgie’s II*, 223 B.R. at 427.

⁸ Kir Temecula urges only the ministerial act of completing the levy remained. This is incorrect because the levy is void. *See In re Gruntz*, 202 F.3d 1074, 1082 (9th Cir. 2000)(confirming that acts taken in violation of the automatic stay are void).

1 Alternatively, Kir Temecula should have sought an order lifting the stay to permit it to
2 levy the Debtor's assets if this was the route it chose to take.

3 **IV.**

4 **CONCLUSION**

5 Kir Temecula's motion is denied. Kir Temecula is not entitled to turnover
6 of the funds in the bank account; nor is it entitled to immediate payment from any of
7 the estate's other assets. Kir Temecula's claim is not entitled to superpriority
8 notwithstanding the portion of the Surrender Order that directed immediate payment.
9 Its claim shall be paid *pro rata* with the other unpaid chapter 11 administrative claims
10 to the extent that any assets remain. This Memorandum Decision is in lieu of findings
11 of fact and conclusions of law. Counsel for the Trustee shall prepare and lodge a
12 separate order in accordance with this memorandum decision within ten days of the
13 date of entry.

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16 Dated: _____

17 LOUISE DeCARL ADLER, Chief Judge
18 United States Bankruptcy Court
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24 CAD 168
25 [Revised July 1985]

26 UNITED STATES BANKRUPTCY COURT
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1 SOUTHERN DISTRICT OF CALIFORNIA

2 In re Bankruptcy Case No(s). 00-00742-A7
3 Case Name: In Re: LPM Corporation, etc., et al.

4 CERTIFICATE OF MAILING

5 The undersigned, a regularly appointed and qualified clerk in the Office of the
6 United States Bankruptcy Court for the Southern District of California, at San Diego,
7 hereby certifies that a true copy of the attached document, to-wit:

8 MEMORANDUM DECISION

9 was enclosed in a stamped and sealed envelope and mailed to the following parties at
10 their respective addresses listed below:

11 Attorney for Debtor

12 L. Scott Keehn
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22 The envelope(s) containing the above document was deposited in a regular United
23 States mail box in the City of San Diego in said district on September 29, 2000.

24 _____, Deputy Clerk
25 CAD 168 Roma London